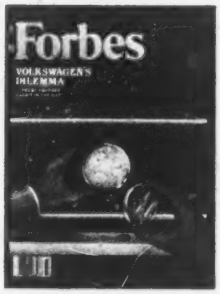
Forbes

VOLKSWAGEN'S DILEMMA

IS THERE ANOTHER RABBIT IN THE HAT?

SAMPLE 22DC
DC 20014

August 17, 1981
Volume 128,
Number 4



71 Cover Story: Why isn't the pioneer of well-made small cars sitting on top of the world?

36 Rupert Murdoch: "I don't see any fun in wiring up a lot of homes. The way to make money is to buy a cable franchise and sell it quickly."

56 Firestone: The liquidity crisis is over. But at what cost?

31 Companies:
Time Inc.
The real story is not the inevitable death of the Washington *Star*. The real story is that Time is now more a cable television company than anything else, and one with vast hidden, and undervalued, assets.

33 Unemployment:
The Hidden Cause
Why do companies that try to stabilize employment wind up subsidizing those that don't? Because the unstable ones seem to have a lot of political clout.

34 Companies:
Aetna Life & Casualty
It's not nearly as conservative as it may seem. Just different.

35 Investing:
Henry Singleton Scores Again
Teledyne's chairman is still running his company like a personal investment portfolio—and still picking the right stocks.

36 Publishing:
A Talk With Rupert Murdoch
For 30 years, people have been underestimating him. But his worldwide newspaper empire is now nearly as big as the New York Times Co. and Dow Jones combined.

37 Pharmaceuticals:
Here They Come Again
Sankyo, Shionogi, Takeda and Fujisawa are not exactly household names in the U.S. drug industry—yet.

42 Companies:
Georgia-Pacific Corp.
The market has been treating this onetime growth stock favorite like a has-been. Is it? Or has Wall Street mistaken good sense for stagnation?

44 Regulation:
The Swimming-Pool Slide Monopoly
Bureaucratic action created it; bureaucratic inaction preserves it.

46 The Up-And-Comers:
Boston & Maine Railroad
Timothy Mellon, 38, is one of *those* Mellons, but he's hardly your rich playboy. Consider his dream of uniting New England's fragmented railroads.

51 The Up-And-Comers:
Welbilt Electronic Die Corp.
"Everybody's running away from the South Bronx," says John Mariotta, "and I need more room!"

56 Companies:
Firestone Tire & Rubber Co.
The blood has been running in the gutters in the two years since John Nevin took over, and there may be more to come. What he's looking for is the day he can say, "Damn! It worked!"

58 Companies:
Arkansas Best Corp.
"I didn't want to be just a survivor," says H.L. Hembree. "I wanted to *achieve*."

64 Companies:
Wolverine Worldwide
Not long ago its advertising slogan, "Hush Puppies are dumb," seemed more candid than clever. These days, the basset hound is considerably less doleful.

65 Tax-Exempt Bonds:
You Scratch My Back . . .
How Forsyth, Mont. (pop., 2,800) got its new swimming pool built—and what it all has to do with industrial pollution.

71 Cover Story:
No More Rabbits In Volkswagen's Hat
The world's biggest builder of small cars is facing a future of inflated wage costs, stagnant productivity and erosion of export markets. The implications are ominous for Detroit as well as for Wolfsburg.

78 The Numbers Game:
The Inscrutable CPA
There are 400,000 manufacturing concerns in China and one accounting firm. The Chinese are trying to do something about it, but it will not be easy.

82 Taxing Matters:
There Is No Free Lunch
Or is there?

83 Companies:
Rohr Corp.
Carl L. Sadler was once a Rohr director. Now he's its CEO. Retributive justice, some might call it. Including Carl Sadler.

46 *The Up-And-Comers: But what would grandpa say?*

64 *"The old Hush Puppy has come a long way," says Tom Gleason. Maybe it's time to retire that slogan about being dumb.*

120 *The Streetwalker: If General Tire is in so much trouble, why doesn't "investor" Charlie Bluhdorn sell while he's ahead?*

Faces Behind The Figures

95 James E. Lee,
Gulf Oil Corp.
95 James M. Schlatter,
G.D. Searle & Co.
95 David L. Luke III,
Westvaco
96 John Hummer,
Niederhoffer, Cross & Zeckhauser, Inc.
96 Jack Armstrong,
Imperial Oil, Ltd.
97 Sir John Treacher,
Playboy International
97 Ralph Ginzburg,
Avant-Garde Media, Inc.
100 Jackie Presser,
Teamsters Union
100 Craig A. Nalen,
Overseas Private Investment Corp.

102 Personal Affairs
The ancient practice of barter has become a huge component of the underground economy. Also: The high cost of headhunters, "in-plant" travel agencies, some yardsticks for variable-rate mortgages and the passport bottleneck.

115 Statistical Spotlight: The Downers
The analysts are scrambling to revise their earnings estimates. And most of the revisions are downward.

117 The Funds; Life Insurance Investors
With all its assets in life insurance companies, John Gardner's Topeka-based mutual fund led the industry in the first quarter. So he's bailing out while he's ahead.

118 The Money Men: Richard Young
The sage of Newport looks like an aging altar boy and is as tough as a sailor on shore leave. What he has been saying of late has been remarkably accurate.

119 The Streetwalker: RCA, General Tire, Rank
The news is so bad, maybe it's time to buy: Doesn't Charlie Bluhdorn see all those potholes? And "an asset-stripping situation beyond belief."

Money And Investments

25
What's Ahead For Business?

26
The Forbes Index

111
The Forbes/Wilshire 5000 Review

Columnists

125
Ben Weberman

126
Heinz H. Biel

127
John Train

128
Richard B. Hoey

130
Stanley W. Angrist

132
Srully Blotnick

Departments

4
Side Lines

8
Trends

10
Follow-Through

15
Readers Say

19
Fact and Comment

22
Other Comments

134
Editorial Index

135
Flashbacks

136
Thoughts

Photos:
8, Owen Franken/Sygma; 10, Doug Wilson/Black Star; 20 bottom, Kip Cleland; 34, 52, 96 bottom, 97 bottom, Bill Kelly; 36, Robin Lawrence; 42, Rich Iwasaki; 46, Steve Liss/Gamma Liaison; 56, Andrew Sacks/Black Star; 62, Bill Parsons; 64, Ed Bailey; 66, Steve Radue/Forsythe Independent; 84, Jim McHugh; 95 top, Richard Faverty; 95 bottom, Tom Barr/Black Star; 96 top, 106, Pat Pagnano; 97 top left, John Cochran/CanaPress; 97 top right, Vijay; 110, Jerry Flint; 103, Chris Maynard/Black Star; 108, Robert Forbes; 117, Jim Richardson/Black Star; 118, Ivan Massar/Black Star

Illustrations:
33, 38, 120, Philippe Weisbecker; 78, 82, Chas. B. Slackman; 102, Doris Ettlinger

Map:
50, Bob Ritter

Cover:
Mark Hess

Forbes (ISSN 0015 6914) is published biweekly by Forbes Inc., 60 Fifth Ave., New York, N.Y. 10011. Second-class postage paid at New York, N.Y. and at additional mailing offices. Subscription $30 a year, U.S.A. Postmaster: Send address changes to Forbes, 60 Fifth Ave., New York, N.Y. 10011.

Copyright © 1981 Forbes Inc. Title is protected through a trademark registration in the U.S. Patent Office.

WHY THE SIGNALS ARE CONFUSING

WHAT'S GOING ON HERE? Automobile dealers are holding their heads; builders with unsold houses are on tranquilizers; yet many businesses are doing extremely well. The overall result is sluggishness, but no recession. This lopsided economy is caused by the clumsy way we fight inflation. We leave the battle to the Fed, which has only one weapon: tight money. So interest-rate-sensitive industries—especially autos, housing—take all the casualties. And make no mistake: The Fed will hang tough. Menachem Begin has nothing on Paul Volcker.

Certain industries are immune to Volcker's medicine

VOLCKER RECENTLY COMPLAINED THAT "some important sectors of the economy are relatively impervious to direct financial restraint." He listed energy, high technology, services and defense. Volcker is not lusting to cause a depression. He just wishes he had policy instruments that would spread the inevitable pain more evenly. Injured industries plead for relief, but none is in sight. The pent-up demand for credit is tremendous. To create money to meet that demand would send inflation soaring. Only when demands moderate can interest rates come down.

How long, O Lord? The economy peaked in March and is still slowing. Normally credit demand peaks three to five months after the economy. If that precedent were to hold, we could look for lower interest rates soon after Labor Day. However, these are not usual times. Corporate liquidity is extremely low, and once interest rates drop everybody will rush in for long- and medium-term credit; so, too, frustrated would-be home buyers. There was a similar lack of liquidity in the 1973-75 recession, which was almost a year old before interest rates started to trend down, in August 1974. If the 1974 precedent holds we will have to live with historically high interest rates well into 1982.

Credit demand will remain strong long after the economy slows

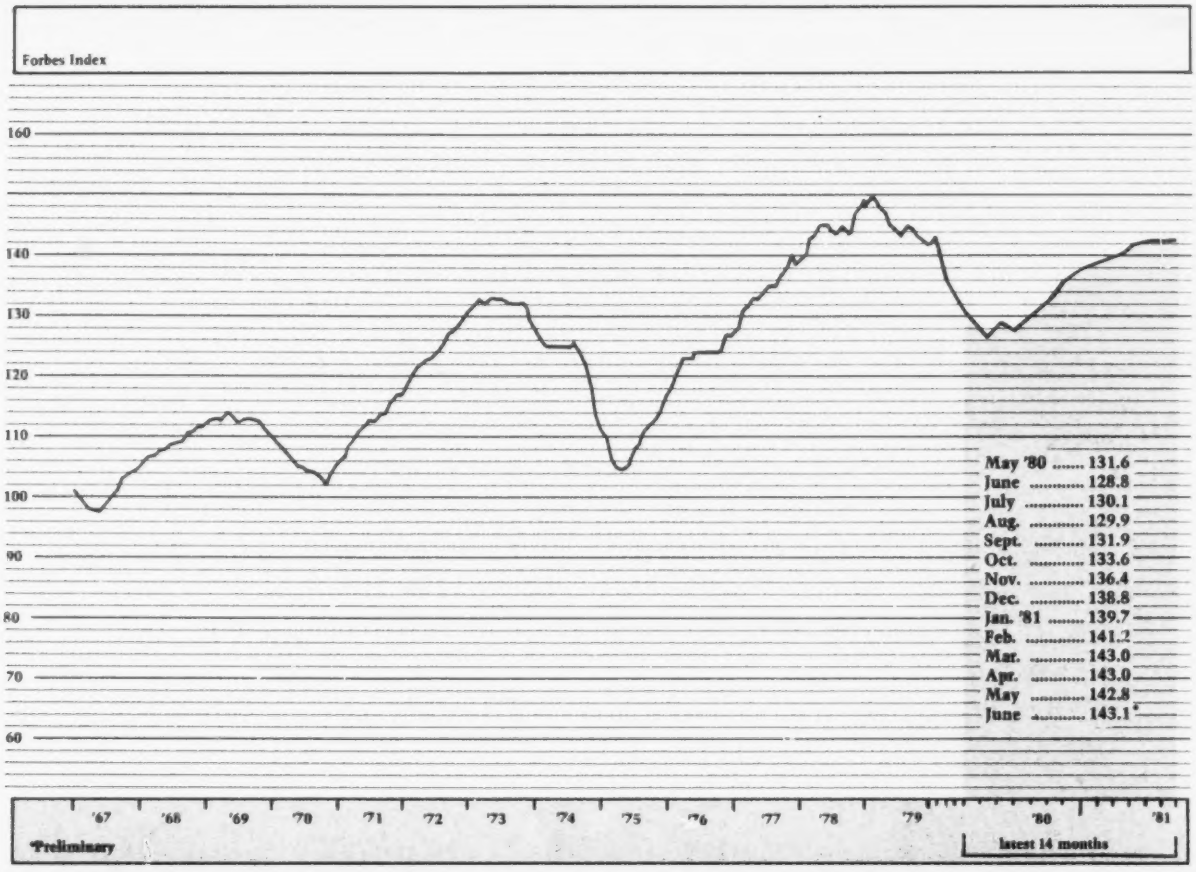
BUT HISTORICALLY HIGH DOESN'T MEAN that the prime rate will stay over 20%. As business remains sluggish, the demand for credit will moderate somewhat.

Many businessmen are now more worried about interest rates than inflation. Paul Volcker doesn't feel that way. So we are getting more relief on the inflation front than on the interest rate front. You hear less about runaway inflation and more about deflation. We're *not* in a truly deflationary situation, but we are making strong progress against inflation. June CPI inflation of 8.4% was far better than it looked. The rate would have been even lower but for mortgage rates, which hardly matter now since so few can afford them anyhow. A recent poll of the influential Federal Open Market Committee members revealed these expectations about 1981 inflation: high estimate, 9%; low, 7.5%.

Little relief in sight for housing and autos

WHAT'S AHEAD thinks the learned FOMC is too cautious; actual price increases could be somewhat slower. Energy is finished, at least for now, as an inflationary factor; interest rates have either peaked or are close to it. Look for interest rates to go down by fall but not way down, and for inflation to continue trending slowly down with an occasional upward blip. Prepare to live with continued lopsidedness in the economy. No auto boom in 1982, no real housing recovery either.

The Forbes Index



The Forbes Index Components

A last hurrah? After a downturn in May, the Forbes Index is rising again—up a slim 0.2%. All that does, however, is to put the Index roughly where it was in April. And even this growth is suspect: Minor readjustments may mean that the final figure becomes a decline. In fact, growth in the Index is caused by only one component: retail sales. They were up 2% in the most recent reporting period.

The FORBES Index is a measure of U.S. economic activity composed of eight equally weighted elements:

Total industrial production

New claims for unemployment compensation

The cost of services relative to all consumer prices

The level of new orders for durable goods compared with manufacturers' inventories

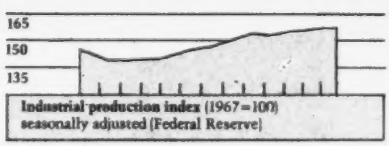
Total retail sales

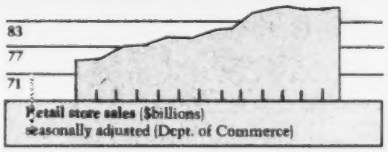
New housing starts

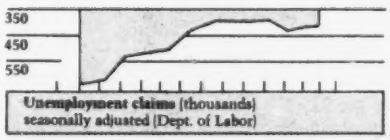
Personal income

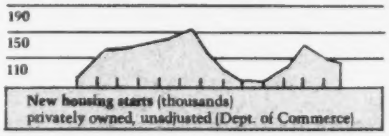
The change in the amount of consumer installment debt outstanding

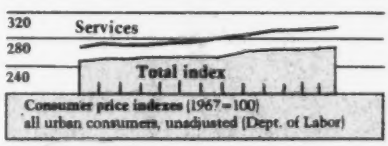
To measure these eight elements, FORBES monitors 11 series of U.S. government data. The last 14 months' data for each series is presented at right.

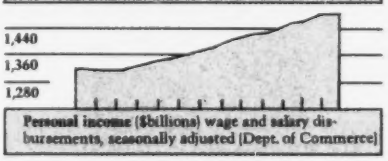


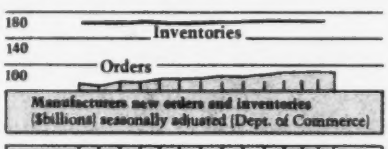


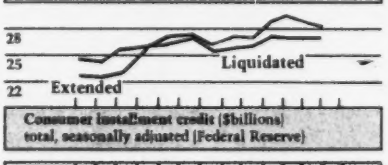












What happens when Peter runs up a tab and Paul has to pay? More joblessness.

Unemployment's hidden cause

By William Baldwin

WOULD WE HAVE less unemployment if unemployment taxes were levied on the basis of how many people a company lays off? Certainly, say economists who have studied the problem. The way it is, they point out, stable industries are subsidizing the others.

For example, take Rhode Island-based machine-tool maker Brown & Sharpe Manufacturing Co. For the past six years it has been straining to keep employees on the job. During the periodic slumps in sales, workers build inventory or learn new tasks. But the company's unemployment taxes keep climbing, reaching $1.1 million last year, or 10 times what former employees drew in benefits. This year taxes will rise again, in spite of a no-layoff policy. The problem is Rhode Island's many employers whose taxes fall short of benefit costs they impose. "We have a socialized system," complains President Donald A. Roach, "and companies like us who try to stabilize employment end up paying for those where there is no attempt to stabilize."

In Rhode Island, jewelry making, the leading manufacturing industry, gets a cheap ride. "It's a seasonal business and there are many small employers who use the system as part of their compensation scheme," Roach says. In Delaware, automakers don't pay their way, so Du Pont picks up part of the cost of the annual furlough for the model changeover. In California the movie industry is one of the big laggards. Almost everywhere, construction does not pay enough.

But don't construction contractors have a rough time in a recession? Or in bad weather? Sure they do, but the fact remains that if you subsidize something, you're likely to get more of it. If construction firms' layoffs were more expensive they might adapt, using weatherproof construction techniques or better work scheduling. To the extent that they could not adapt, the costs would be passed on to customers. That's the way free markets work.

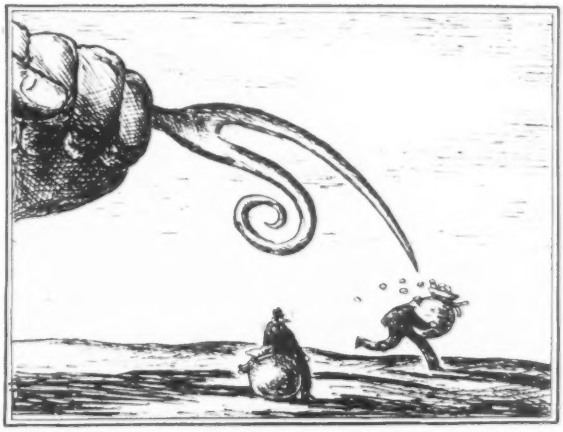
Layoffs would be more expensive if experience rating, in which a company or industry pays for its own unemployment, were the rule. According to University of Maryland economist Frank Brechling: "If we had full experience rating, unemployment would fall."

Then why don't we have it? Because the present system—in which experience formulas are weakened by minimum and maximum tax rates—suits the seasonal industries. And seasonal industries seem to hold more sway over politicians than do stable employers.

Consider the New York legislature, which in 1977 blessed construction with a special 1% discount off the maximum unemployment tax rate. "There was enough pressure exerted politically," says a state labor official. Heavy construction's $13 million in unemployment taxes in 1979 covered only a third of its $38 million in benefits. New York's garment industry paid $45 million for $89 million in benefits that year, thanks to a special 4.3% maximum rate. Finance, insurance and utility companies got stung. New York Telephone paid $14 million in state unemployment taxes, while costing the fund only $876,000. It also paid a disproportionate $3.4 million in administrative costs and "extended benefits," via a flat-rate federal tax currently pegged at 0.7%.

The unions, however, like things the way they are. AFL-CIO economist Bert Seidman opposes experience rating because "it's based on a theory that unemployment is something over which employers have control—and that is clearly invalid." He would prefer that the entire $20 billion-a-year cost of unemployment compensation be funded with a flat-rate tax, a la Social Security.

University of Chicago economist Robert Topel disagrees. He says that employers do have some control over



Out of work and in hock

Thanks largely to maximum unemployment tax rates that let unstable employers off the hook, 14 states and the District of Columbia have had to get bail-out loans from the federal government.

State	Unemployment fund debt to U.S. Treasury (millions)*
Pennsylvania	$1,585
Illinois	1,373
Michigan	1,015
New Jersey	646
Ohio	600
Connecticut	365
Rhode Island	120
Minnesota	114
West Virginia	100
Arkansas	64
District of Columbia	58
Kentucky	52
Delaware	49
Vermont	40
Maine	36

*As of May 31, 1981.
Source: U.S. Department of Labor

temporary layoffs. There are three ways to respond to slack demand, says Topel: Cut prices, build inventory or send workers home. Topel looked at unemployment in 29 industries, statistically stacking states with feeble experience rating, like California and Illinois, against states with strong experience rating, like Texas and Minnesota. His conclusion: Where an individual employer is penalized for layoffs, he tries to avoid layoffs. He says better experience rating could eliminate roughly one-fourth of the country's temporary-layoff unemployment.

Unemployment compensation, however, is a politically touchy subject. Suggest reform and you are accused of being insensitive to the poor or some such sin. Legislators, both federal and state, are eager to appear to be generous while sidestepping the matter of eventual payment. The result is more unemployment, paid for by those who try to avoid laying people off. ■

Those Aetna boys aren't as conservative as they would seem. They are just different.

Listening to its own drummer

IVY-COVERED AND SERENE, the sprawling colonial buildings look like a campus, and John Filer, surveying the world from his majestic 6-feet-4, could be a college dean. But this is the headquarters of Aetna Life & Casualty, the repository of a nice round $36 billion worth of assets, and John Filer its chairman. Ask Chairman Filer whether he plans to follow rival Prudential in buying a brokerage house and he dismisses the idea in almost professorial tones. "You don't," he says, "want to be jumping around with each trend and fad." You get a similar answer when you ask him about the controversial new universal life insurance (FORBES, *July 20*). For now it's not for Aetna. As an aide puts it: "It reminds us of how insurance companies rushed in to buy mutual funds in the Sixties; every one of them got burned."

If you conclude from all this, however, that the gentlemen from Aetna are sitting up there in Hartford, Conn. drowsing over their coupon clipping, you are very much mistaken. Myron Picoult, insurance analyst at Oppenheimer & Co., sums up a good deal of Wall Street thinking when he says: "In its technology investments Aetna shows the aggressive kind of thinking you're not seeing at the other insurance companies."

Aetna's Chairman John Filer
"You don't want to be jumping around with each trend and fad."

Instead of chasing fads Aetna listens to its own drummer, which has led it into satellite data transmission, oil and real estate on a grand scale—most recently in a real estate partnership with Hollywood's Twentieth Century-Fox. Like everybody else, Aetna had problems in real estate in the mid-Seventies, but by last year its realty business and other diversifications provided 11% of Aetna's net profits. In oil, Aetna owns a piece of a $445 million (revenues) Geosource, an oil service business. It has the highest of hopes for Satellite Business Systems, which transmits data via satellite for corporate customers. Right now SBS, a partnership between Aetna, IBM and Comsat General, is nothing but red ink and only three customers on line, but Aetna thinks it will be a $1 billion company by 1990.

Isn't satellite data transmission as much pie in the sky as, say, the brokerage business or universal life insurance? Not the way Aetna sees things. "It is a business that is defined and understood," says John Galvin, Aetna's diversified business head. That's the way Aetna likes things. It doesn't shun risks but wants the "defined and understood."

Wait a minute, though. Isn't Aetna an *insurance* company? It is, and like everybody else in property and casualty, it is having a rough time this year. If inflation weren't problem enough, the insurance companies are being clobbered by sharp lawyers and gullible juries who don't seem to understand that when they hand someone a fat reward their own insurance premiums will eventually reflect the fact.

Basically, an insurance company hopes that premiums and claims will about balance out and that the interest and dividends earned on its reserves will produce a profit. But claims have gotten so far ahead of premiums this year that Aetna is paying out 14% more in claims and operating expenses than it is taking in from premiums—compared with the

and racy writing that has become his trademark.

He moved into the world league in 1969 after he offered to help Britain's Carr family fight off a takeover bid for *News of the World*, the hugely popular and salacious British Sunday paper. Murdoch's master company swapped high-earning, low-asset Australian periodicals for 5.1 million new shares in *News of the World*—giving him more than a quarter of the enlarged equity. He quickly purchased enough additional stock for effective control, and then ousted Sir William Carr as chairman. In the uproar that followed, Murdoch discontinued such Carr indulgences as the company's box at the Covent Garden opera house.

Later that year he maneuvered the International Publishing Corp. (IPC) into selling its losing mid-market London *Sun* to the *News of the World* company. After dropping $30 million over six years under IPC management, the paper was profitable for Murdoch within six weeks. All he paid was $120,000 up front and $1.9 million out of *Sun* profits, and he overtook IPC's London *Mirror*'s circulation in the mid-1970s, hitting 4 million in 1978.

Murdoch's ability to turn properties around quickly has allowed him to buy new ventures with cash flow from existing businesses. Thus the *Sun* and *News of the World* have been the main support for most of his later moves, including the thrust into the U.S. This began in 1973 when a few of Murdoch's companies paid nearly $20 million for San Antonio's *Express* and *News*.

Only four months ago Murdoch seemed as stretched as he had ever been, trying to beat out a series of brush fires in many parts of his empire. In the U.S. his New York *Post*, which he bought in 1976 for $32 million, was still losing money in head-to-head competition with Chicago Tribune Co.'s New York *Daily News*. In London he had gamely taken the reins at the Times group, whose trade union greed and arrogance was notorious even by Fleet Street standards. Worse, the profit-center London *Sun* was suddenly being outshone by a cut-price look-alike, the *Daily Star*.

Characteristic Murdoch toughness has transformed the outlook on all three fronts. The Times unions are much tamer, thanks to Murdoch's convincing threat that he would close the business if the previous anarchy continued. Meanwhile, at the *Sun* there was a problem: political outlook. The *Sun* was backing Prime Minister Margaret Thatcher even while Britain's unemployment mounted. The *Star*, by contrast, is left-ish in its editorial columns if not in its boardroom, and led the hue and cry of unemployment. But Murdoch recovered quickly. The *Sun* suddenly discovered unemployment in its news pages, and, according to Murdoch, the paper has been "flirting" with the new centrist Social Democratic Party.

In the *Star-Sun* war, Murdoch also showed that he is a dangerous man to cross. He raised the price of the *Sun*, expecting the *Star* to follow; it didn't, and gained circulation at Murdoch's expense. Murdoch countered with a vicious price war in which the rival *Star* finally conceded defeat.

The New York *Post* venture has departed from the usual script in that it is losing a lot of money—$12 million last year, with the outlook no better for this year. But Murdoch says he will fight three or four more years because the prize, as he sees it, is New York's popular newspaper market—nearly 5 million readers.

When he bought the *Post*, it was a sleepy evening paper breaking even with a sale of 500,000. The much bigger *Daily News*—circulation 1.8 million—was selling only in the morning. Hostilities heated up last year when the *News* started an evening edition. Characteristically, Murdoch replied with a morning edition. It was conceived as a shot across the *News*' bow—but the *Post*'s morning operation has gone much better than Murdoch expected. He has been gloating as the *News*' circulation has sagged and the man brought in to raise the tone of its evening edition, former *New York* magazine editor Clay Felker, is out. Says Murdoch of the 3,000-word New Journalism pieces Felker imposed on *News* readers: "They introduced types of journalism that had no place in a newspaper, let alone in a *popular* newspaper." Murdoch would never make the mistake of trying to impose his tastes on his customers.

He now sees the Manhattan battle as a fight to the finish. "We are not large in the market but competitively we are everything because we are stopping the *News* from recovering its costs. It has about 4,700 employees, 90% of them on firm tenure. We have 1,100." Every Harvard Business School student learns—and every gut businessman is born knowing—that in a knock-down-drag-out business fight, the man with the lowest costs nearly always wins.

Can Murdoch beat the *News*, until recently the U.S.' biggest-circulation daily and once the master of popular journalism? However long they once looked, the odds now look very much in Murdoch's favor. One awed former lieutenant reckons that anything is possible. "Murdoch sees around corners," he says. He doesn't, of course, but what he does do is see the newspaper business more clearly than anyone else in the world. ■

First television sets, cameras and steel. Then autos and computers. Now those tough competitors from across the Pacific are aiming at the drug industry.

Rx: made in Japan

By Carol E. Curtis

GREEN CROSS, a middle-size Japanese company, will soon start selling artificial blood—a major pharmaceutical breakthrough. Sankyo, based in Tokyo, is already a leader in anticancer drugs. Two of the best new antibiotics to come on the U.S. market, Moxalactam and Cefizox, were developed by Shionogi and Fujisawa.

At the moment, of course, those obscure names are hardly the medical equivalents of Nissan and Toyota. Japan's international sales account for a mere 3% of its total drug revenues—mostly in the form of bulk pharma-

ceuticals—and U.S. companies get 40% of their revenues from overseas sales. Still, the $15 billion-a-year Japanese drug industry is preparing an impressive marketing offensive.

Penetrating the U.S. drug market is a key element in that effort. With the prospect of limited increases in auto and consumer electronics exports, Japan needs high-growth replacements. Pharmaceuticals, like semiconductors, are easy to transport and just the kind of high-value-added products that appeal to government planners.

Look out, Lilly and Merck

Japan's leading pharmaceutical companies are largely unknown to the U.S. public. American drug companies, however, are getting to know them very well.

Company	Revenues* (millions)	Major product lines
Takeda	$1,826	antibiotics, vitamins
Sankyo	695	anti-ulcer and anticancer drugs
Fujisawa	605	antibiotics, nervous system drugs
Shionogi	577	antibiotics, nervous system drugs
Tanabe	461	circulatory and respiratory drugs
Eisai	400	circulatory and respiratory drugs
Taisho	335	nonprescription tonics, nutrients
Yamanouchi	333	antibiotics, tonics
Chugai	310	anti-ulcer and anticancer drugs
Daiichi	290	vitamins, tonics

*Exchange rate: 230 Yen = $1 *Source: Scudder, Stevens & Clark*

Not surprisingly, Japanese firms started emphasizing product development about a decade ago. In 1965 the average Japanese drug company spent 1% of sales on research. Today it spends about 7.5%—almost even with the U.S. "The most important thing in drugs is successful research, and the Japanese are doing very well at it," says William Holzer, a Japan specialist with Scudder, Stevens & Clark in New York.

Such big spending, however, provides an even greater incentive to export. "To develop a new drug takes ten years and $9 million," says a Tokyo analyst. "That means you can't depend only on the Japanese market."

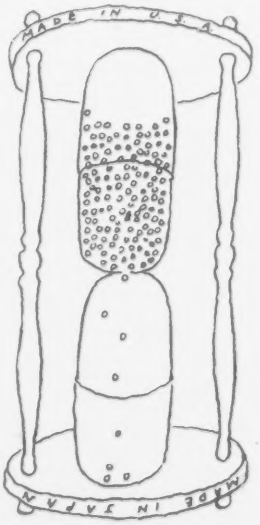
Japan has been steadily increasing its foreign drug introductions—a key statistic since most new products are launched outside the U.S. Japanese revenues from drug-licensing agreements with foreign countries over the last decade have nearly quadrupled, while U.S.-manufactured drugs have been licensed overseas at a slower pace. Robert Schmitt, an analyst at Drexel Burnham Lambert who has been following Japanese industry for 16 years, believes Japan is now preeminent in anticancer drugs, certain antibiotics and artificial blood. Says Schmitt, "They are gearing up to become a world leader."

The Japanese government—no novice at encouraging exports—is actively assisting. Last year the Pharmaceutical Affairs Act extended the time a company can market a drug under exclusive license from three to six years. A change in the patent system, extending coverage to compounds as well as processes, has also encouraged more innovation.

Japanese companies are rushing to patent their drugs in the U.S., too. In 1963 Japan ranked fifth in the number of foreign-origin drug and medicine patents issued in Washington, with 350. In 1977—the most recent period for which data are available—the Japanese had 1,700 drug and medicine patents in the U.S., second only to West Germany.

Still, Japanese entry into the U.S. drug market isn't likely to be a repeat performance of their conquest of the auto industry. Though Detroit has relatively few product lines, the average drug company has at least 12—making it tough to compete across the board. What's more, the U.S. drug industry is not monolithic: The 149 members of the Pharmaceutical Manufacturers Association account for 90% of domestic prescription drug sales. "Pharmaceuticals are a series of small, overlapping monopolies," explains Paul Brooke, who follows the industry for Cyrus J. Lawrence.

Prescription products sold in the U.S. must, of course, be approved by the Food & Drug Administration, a process that can take as long as a decade. But the current FDA policy of approving more new drugs—without regard to origin—works to the advantage of foreigners. "Companies now scramble on an equal footing," says Kenneth Peterson, a vice president of research at Scudder, Stevens & Clark. As a result, he adds, "U.S. research and development has lost its secure franchise on the drug market."



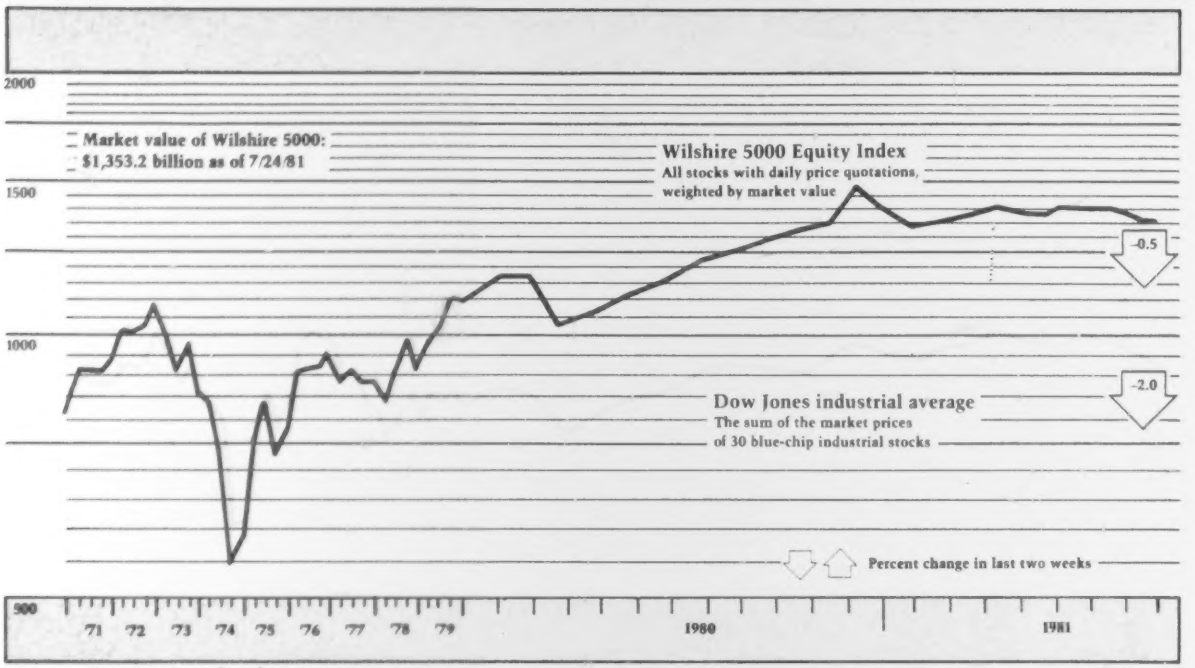
FDA approval, though, is only the beginning. A marketing organization, with a large sales force, is essential for a real export push, and until recently the Japanese chose to participate in the U.S. market almost exclusively through licensing agreements. Typically, these agreements grant a company like Pfizer or SmithKline the right to produce, package and sell a drug in exchange for paying the Japanese company a royalty. Now the Japanese are moving more aggressively and trying joint ventures. Says Barry Cohen, a spokesman for Abbott Laboratories, "The next step is likely to be independent participation in the U.S. market."

Abbott, for example, is currently joint-venturing with Takeda, the largest Japanese drug firm, in developing five different products. By 1984 all five are expected to be on the U.S. market. Other joint ventures include SmithKline and Fujisawa, Lilly and Shionogi, and Merck and Banyu.

The Japanese have been gun-shy so far about making direct acquisitions of U.S. drug companies. Mitsubishi recently bought 10% of tiny ($23 million) Key Pharmaceuticals, but aside from a few industry giants like Takeda, most Japanese drug firms are small in comparison with their American counterparts and thus unable to tackle a major acquisition. "The form expansion will take," predicts Scudder, Stevens' Peterson, "is to joint-venture with a U.S. company, then take control."

Are American companies beginning to feel the heat? Giants such as Johnson & Johnson, Lilly and Merck are financially robust and big research spenders. But they also cast wary eyes to the East. Merck's Chief Executive John Horan acknowledges the threat—but isn't worried. "The U.S. industry," he says, "is fully competitive." A Pfizer executive sees things differently. "Whether General Motors or Ford would have envisioned the extent of Japanese penetration five years ago, I really don't know. I think we're in that same situation." ■

The Forbes/Wilshire 5000 Review



Is a market bottom in sight? Although stocks continue to lose ground, the most recent two-week slide was much gentler than the early July decline. The market as measured by the Wilshire Index was down only 0.5% over the period—compared with the preceding 3.4% slump.

Another sign that the summer doldrums may be ending is trading volume. In the most recent two-week period, Big Board volume was 4% less than it was in the earlier period after adjusting for one less trading day. This suggests that there are fewer sellers looking to dump stock. Factor out the frenetic activity in energy issues fueled by merger-itis, and Wall Street may be approaching what some technical analysts see as a support level.

On a fundamental basis, investors are receiving mixed signals: Red lights warn of an economic slowdown, high interest rates and weakness in earnings. Some green lights: prospects of a tax cut and reduced federal spending, cheaper energy, higher retail sales. Still, until the economy shows clear-cut direction, the predominant mood is likely to be neither bullish nor bearish.

In the meantime, the market is retrenching to a conservative middle ground. High-volatility, high-growth, high-P/E and low-yield stocks are backing off more than their counterparts. Yet the blue-chip issues are also being punished. In the most recent two weeks, the Dow fell almost twice as far as any of the other market indicators.

Close-up On The Equity Markets

Performance of five leading indexes

Percent change	Wilshire 5000	Dow Jones industrials	NYSE Composite	ASE Market Value Index	NASDAQ Composite
in last 4 weeks	–3.2	–5.7	–3.1	–3.2	–5.4
in last 52 weeks	10.5	2.0	8.0	15.9	22.6

Stock performance based on five key investor yardsticks

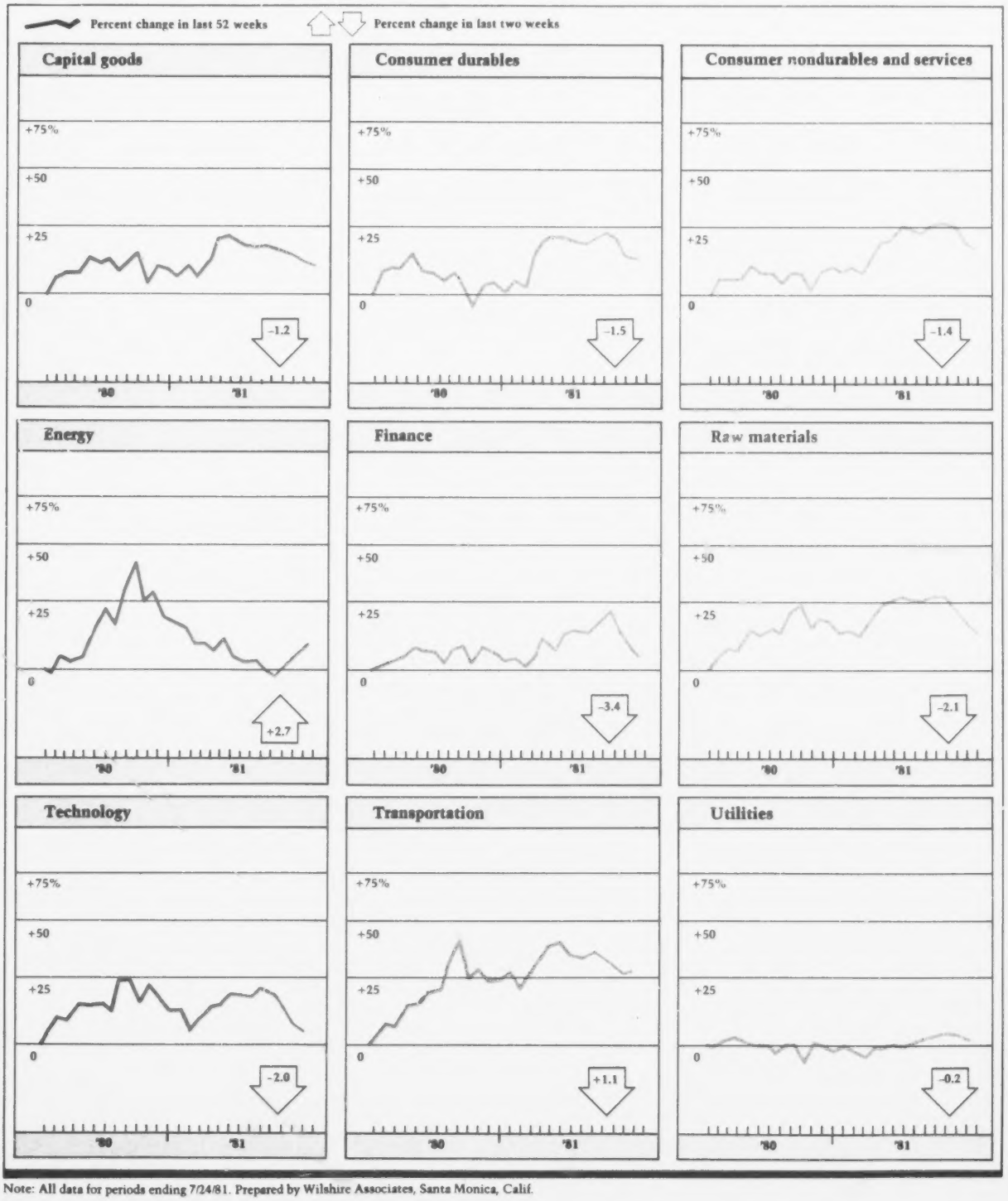
Percent change	Volatility *		P/E multiple		Dividend yield		Growth profile†		Share price	
	high	low	over 25	under 5	over 7.5%	none	high	low	over $40	under $4
in last 4 weeks	–6.4	–2.2	–6.0	–2.7	–2.8	–4.6	–5.1	–3.7	–3.5	–4.0
in last 52 weeks	39.9	11.6	33.7	20.7	4.8	38.0	36.3	15.9	13.7	42.4

* A stock's sensitivity to overall market movement. High-volatility issues have wide price fluctuations; low-volatility issues are more stable.
† A quantitative evaluation of a stock's growth image, determined by Wilshire Associates.

Note: All data for periods ending 7/24/81. Prepared by Wilshire Associates, Santa Monica, Calif.

A spotlight with a narrow focus. The battle for Conoco is focusing Wall Street's attention on energy. Other companies may also be up for grabs. In fact, the limelight is now being extended to asset-rich railroads. Transportation was the only group other than energy to finish the last two weeks in the black.

On a 52-week basis only the transportation stocks have produced returns better than money market funds. Support for the railroads and a lift-off of airlines from their low-altitude performance of early 1980 have helped. If the economic downturn worsens and rail shipments and passenger levels drop, however, transportation stocks are vulnerable. As we report elsewhere *(see p. 115)*, analysts are scaling back earnings projections for airlines and trucking companies. Other groups that may be hurt by declining profits include finance and technology.



Note: All data for periods ending 7/24/81. Prepared by Wilshire Associates, Santa Monica, Calif.

NOTE

ONLY THE FOLLOWING PAGES OF THIS

PUBLICATION HAVE BEEN FILMED

Cover 1, p. 4-5, 25-26, 58-
62, 64-66, 68, 70-72, 77-
79, 81-82, 84, 86-87.